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DCI MEMO CONTRIBUTION — (Back-up paper)

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Industrialized Countries: Medium-Term Economic Prospects

All OECD economies have been under serious economic strain in 1982, and although recovery is expected in 1983, it will be substantially weaker than pervious postrecession upturns. Consequently, friction among developed countries over economic policies is likely to increase, particularly when governments believe that jobs may be at stake. Protectionism, export subsidies, and competitive devaluations could all play a part in these conflicts. 25X1

Declining but still high real interest rates, stemming in large part from the combination of expanding budget deficits and restrictive monetary policies, are expected to remain a major obstacle to vigorous economic growth. The availability of substantial excess capacity will further discourage investment. Moreover, recent surveys indicate that consumers in many countries are not yet ready to increase their purchases of big-ticket items. 25X1

This year OECD GNP will probably fall slightly, down from 1.2-percent growth in 1981; for the non-US OECD, real GNP growth is expected to slip from last year's 0.8 percent to 0.6 percent. Final domestic demand probably will continue to be weak, with private and public consumption growing by less than 1 percent in the major industrial nations and fixed investment posting a small decline. Falling oil and raw material prices, however, should help these economies. 25X1

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The brightest spot on the economic scene is the downturn in inflation. For the OECD as a whole, consumer prices are expected to rise by less than 8 percent, the smallest annual increase since 1978. The improvement will not be uniform, and in some countries--such as France, Italy, Greece and Spain--large budget deficits, rapid money supply growth, and further currency depreciation will sustain double-digit rates. 25X1

In addition, the OECD's current account deficit should decline dramatically because of the recent drops in prices of imported raw materials; the overall shortfall may dip below $10 billion--roughly one-third the combined 1981 deficit. Individual performances will vary substantially this year, with Japan and the United Kingdom running hefty surpluses, while the French current account deficit will deteriorate further to $7 billion.

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Mounting unemployment is the most serious economic problem. By yearend 1982, total OECD unemployment could reach 29 million--about 15 percent above the 1981 level. In several countries, unemployment rates will remain well above 10 percent; British unemployment stood at 12.8 percent in October, and about 16 percent of the Spanish labor force is idle. 25X1

New economic stimulus, however, would intensify already serious budget deficits. Monetary policies have eased only slightly this year as central banks tried to contain the inflationary impact of budget deficits. In France, the government deficit will be more than 3 percent of GNP this year, after averaging less than 1 percent in 1960-80. Deficits could exceed 10 percent of

GNP in several countries, including Italy, Denmark, and Ireland. In most of these countries, high unemployment has boosted the cost of generous social welfare programs, while the recession has held down revenue growth. At the same time, high interest rates have increased debt-service burdens. 25X1

We expect some improvement in economic performance in 1983, with the increase in GNP averaging 2 percent for the OECD. Even this low rate of economic growth could be stymied. Non-OPEC LDC debt problems may curtail import spending, while OPEC countries continue to curb imports due to the accumulated effect of slack oil demand. The outlook for next year assumes that nominal oil prices remain at roughly the 1982 level, that monetary and fiscal policies do not change significantly, and that exchange-rate adjustments will be limited. Under this scenario, the OECD current account probably will remain in deficit, and inflation should slow further. Unemployment would remain a serious problem, particularly in Western Europe. 25X1

The strength of the US economy--which we assume will grow by about 3 percent in 1983--remains a key to the shape of the economic recovery in the rest of the OECD. We estimate that a 1-percentage-point change in US GNP growth would change GNP growth in the other OECD countries by about 0.2 percentage point. If the US recovery is weaker than expected, non-US OECD growth would fall below the 1.6 percent now projected for 1983. 25X1

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OECD: GNP Growth

Percent

	1981	1982	1983
OECD	1.2	-0.1	2.0
United States	1.9	-1.5[a]	2.9[a]
Non-US OECD	0.8	0.6	1.6
Big Six	0.8	0.5	1.4
Japan	2.9	2.2	3.1
West Germany	-0.3	-1.0	Negl
France	0.2	1.0	0.9
United Kingdom	-1.2	1.1	2.0
Italy	-0.2	0.4	2.0
Canada	3.1	-4.0	2.0
Small Seventeen[b]	0.9	0.8	2.0

[a] Forecast from the Data Resources, Inc. November simulation of the US economy.

[b] Australia, Austria, Belgium, Denmark, Finland, Greece, Iceland, Ireland, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, and Turkey.

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